

March 11, 2004

Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Docket No. R-1176
Availability of Funds and Collection of Checks

Dear Ms. Johnson:

World Savings Bank, FSB (“World”) is a federally chartered savings bank headquartered in Oakland, California, with \$80 billion in assets, and operates 275 savings branches in ten states serving over 600,000 households. World is a wholly owned subsidiary of Golden West Financial Corporation. World is pleased to comment on the Federal Reserve Board’s (the “Board”) proposal¹ to amend Regulation CC to implement the provisions of the Check Clearing for the 21st Century Act (“Check 21” or “the Act”).

World generally supports the Board’s proposed regulations and commentary implementing Check 21. In the interest of brevity we will comment only on those proposals for which World strongly recommends a specific and/or different approach. Page references are to the Board’s request for comments. The term “IRD” (Image Replacement Document) is used here interchangeably with the term “substitute check.”

ENDORSEMENTS (pages 11-13)

The board requests comment on all aspects of the proposed endorsement and identification standards listed:

- a. Because an original check is reduced in size when it is converted into a substitute check, the location of an endorsement, particularly a depository bank endorsement, sprayed on an original paper check likely will change. The Board believes that a reconverting bank should bear the liability for any losses that result due to the shift in the placement of the endorsement.
 - In the case when a substitute check is returned to the depositor for endorsement issues (missing, wrong, etc.), World is concerned there will not be enough room for the person to sign the back of the substitute check without interfering with any of the endorsement positions, nor may there be enough room in the image area itself. If the

¹ 69 Federal Register 1470 (January 8, 2004)

- newly supplied endorsement does exceed the image area, the reconverting bank should not bear liability for losses that result.
- b. The Board is proposing to require returning bank endorsers to comply with the same endorsement requirements as collecting banks. Specified endorsement elements must appear on the back of a substitute check that is returned. The Board requests comment on what benefits, if any, there would be in providing returning banks with the flexibility to indorse on the front of checks and to include additional information in their endorsements.
- World believes Appendix D should allow for Region 7F on the substitute check (referring to IAW DTSU 9.90) to be utilized in a return to remain consistent with all governing rules.
 - Allow a carrier or re-stripping to be used when returning a substitute check to allow flexibility to properly encode the "5" in position 44. This would avoid the creation of a second IRD and the possibility of having two legal documents in the payment stream.
 - We see no benefit to placing new information on the front of the item when processing a received substitute check for return and not creating a qualified return IRD. Using the front for endorsement information could obscure critical features that need to remain legible, such as the maker's signature, payee name and amount.
- c. The Board proposes to amend Appendix D to require a paying bank that is also a reconverting bank with respect to a substitute check to identify itself as such by placing on the back of the check its RT number (without arrows) and an asterisk at each end of the number. This is to preserve the bank's identity and would not constitute an endorsement.
- We agree that the creator of the substitute check should be identified. Additionally, we request clarification on the proper endorsement of a returned substitute check that is re-deposited. It is unclear whether the depositing financial institution should endorse the item as the 2nd bank of first deposit (>RT<), or whether it would be a subsequent endorser (*RT*) since the IRD already carries the warranties supplied by the creator of the IRD. Alternatively, the depositing financial institution might be considered the 2nd bank of first deposit and also the reconverting bank (>*RT*<) since they are forwarding this item for presentment after receiving it back from their non-bank customer. There is room for fraud when the IRD leaves the collection process and is returned to the customer, then presented for redeposit. The creator of the IRD should not be responsible for any fraud that occurred while the item was in the hands of the depositor.

PURPORTED SUBSTITUTE CHECKS

The Board requests comment on whether an item that fails to meet any of the other substitute check requirements in 229.2 (zz) also should be treated as though it were a substitute check for those limited purposes.

- World urges the Board to delete section 229.51(c), the purported substitute check provision, from the final rule. World supports the comments of America's Community Bankers on this subject. We echo their recommendation to eliminate the concept of "purported substitute checks" and to allow MICR-line repair by collecting and paying banks without compromising the item's legal equivalence. This would enhance the integrity of substitute checks, and save banks having to explain to a customer that a substitute check may not be the legal equivalent of an original check under certain circumstances, even though it bears a legend stating that it is.

ACH DOUBLE POSTINGS (page 16)

The Board requests comment on whether using information from a check to create an ACH debit entry should be a payment request covered by the substitute check warranties.

- No, using information from a check to create an ACH debit entry should not be a payment request covered by the substitute check warranties. Such "check conversions" are coded on their way through the payment system as electronic transactions governed by an existing scheme of NACHA rules and the Board's Regulation E, and should remain subject to those already-existing rules and regulation. ACH debits are outside the scope of Check 21's warranty against double debits.

MULTIPLE SUBSTITUTE CHECKS IN A CLAIM (page 22)

The Board requests comment on whether additional commentary to 229.54 (claims for multiple substitute checks in the same communication) would be useful and, if so, what specific points should be covered.

- World recommends allowing a bank at its discretion to require a separate claim statement for each disputed item. In this case the bank would not treat multiple items as one claim and would make a separate determination as to validity and recredit for each item.

MODEL DISCLOSURES (page 28)

The Board requests comment on whether the proposed model customer disclosure C-5A is clear, accurate and concise.

- The disclosure is clear and accurate but it is too long for an initial disclosure about substitute checks. We would recommend that the Board shorten the disclosure by dividing it into two parts and allow banks the discretion to provide the first and second

part of the disclosure to customers at different times appropriate to their need for the information.

- The first part of the disclosure (the first four sections through the section titled “Expedited Funds,” plus information about how to contact the bank to make a claim) would be distributed to existing deposit customers and provided to new deposit customers to inform them about substitute checks in general.
- The second part of the disclosure (“How to Make a Claim...” through “Reversal of Refund”) would be provided to a customer by the bank when the bank responds to a claim the customer makes with regard to a substitute check. The claim and response information is useful and meaningful to the customer at that time but could be overlooked or discarded if provided earlier.
- In any case, the language of “How to Make a Claim for an Expedited Refund”, should be edited to say, “(1) The date that we mailed or delivered the account statement showing the charge...” to match the commentary to section 229.54(b).

The Board requests comment on whether providing model language for the 229.54(e) (response to a consumer’s expedited recredit claim) notices are useful.

- We agree that model language for the notices would be useful.
- We suggest that the Board state that it is providing the model language to assist banks in complying with the notice requirements of the Act.

OTHER ADMENDMENTS TO REGULATION CC (pages 28-29)

The Board is proposing several amendments to Regulation CC and its commentary that are unrelated to the Check 21 Act. The Board requests comment on each of these proposed revisions and also welcomes comments about any other areas of the existing rule and commentary that should be clarified. World appreciates the opportunity to offer the following comments:

- World generally supports the proposed revisions, except as noted to the contrary below.

Section 229.30 Paying Bank’s Responsibility for Return of Checks

- World opposes the extension of the midnight deadline. It appears there could be multiple cutoff times to manage.

Section 229.33 Notice of Nonpayment

- We do not agree to reduce the time frame for providing notice of nonpayment because the current deadlines are manageable.

Specific Requests for Comment

APPLICABLE INDUSTRY STANDARDS

The Board requests comment on the desirability of including only a general reference to generally applicable industry standards in the rule text. In cases where only one industry standard applies, the proposed commentary would identify that standard. Is the approach satisfactory or would we prefer that the Board identify specific industry standards within the text of the rule at all times?

- This approach is satisfactory. We prefer the flexibility to list the applicable standards in the commentary rather than the rule. This will allow the Commentary to incorporate standards changed or created by new technology.

REMOTELY-CREATED DEMAND DRAFTS

- We strongly support incorporating into Regulation CC the U.C.C. revisions regarding remotely-created demand drafts.
- We believe that the definition should apply to all remotely-created demand drafts drawn on consumer and fiduciary accounts (such as accounts managed by Conservators, Executors, and Trustees).

RELATION OF THE CHECK 21 ACT TO OTHER LAW

The Board specifically requests comment on whether the proposed commentary is adequate with respect to the interaction between the Check 21 Act and existing law or whether commenters believe that additional discussion and examples are needed.

- World believes that the proposed commentary to section 229.54(a)(2) goes beyond the scope of the Act by incorporating U.C.C. warranties into the area of expedited recredit for substitute checks. The incorporation of state law warranties into the expedited recredit scheme is not appropriate for two reasons. First, it gives recipients of substitute checks different and new protections not available to customers who receive paper checks. This makes substitute checks not just legally equivalent but legally superior to paper checks, contrary to the intention of the Act. Second, there are already valid existing procedures for resolving disputes related to breach of U.C.C. check warranties (such as claims for forged or altered items) in which the rights of customers, paying banks and depository banks are well-defined. To superimpose the expedited recredit scheme would simply create confusion in the dispute resolution process.

- Check 21 provides consumers with the expedited recredit remedy for losses incurred because they received a substitute check rather than an original. Under Section 5 of the Act, a depository institution that transfers, presents or returns a substitute check warrants that the substitute check (1) meets the requirements for legal equivalence and (2) is not a duplicate of a check that has already been paid. The expedited recredit remedy is available to a customer who needs help from his or her own paying bank to obtain a “legal” substitute check and/or a quick remedy for a duplicate debit that has occurred against his or her account. It is not necessary for the Board to go beyond the Act and extend the expedited recredit remedy to other situations that have other adequate remedies in place under existing law.
- Since the warranty claim with respect to a substitute check is limited, we request the Board to eliminate the portion of the proposed commentary that allows a consumer to make an expedited recredit claim for a breach of a U.C.C. warranty.

ADDITIONAL ITEMS THAT NEED CLARIFICATION

- World recommends that the definitions of “truncate” in Section 229.2(ccc) and “truncating bank” in Section 229.2(ddd) be revised to delete references to substitute checks. A truncating bank should continue to be defined as a bank that removes an original check from the payment stream and converts it into electronic form. Creation of a substitute check is not truncation as currently understood in the processing arena, because a substitute check never loses its character as a paper item.

In conclusion, World appreciates the opportunity to comment on the Board’s proposals for implementation of this important legislation. Thank you for your attention. Should you have questions regarding our comments to the proposal, please contact either Lori Cutler, 210-543-4436, lcutler396@worldsavings.com or Carla Rush, 210-543-5172, crush258@worldsavings.com.

Very truly yours,

/s/

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